

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name City of Benton Harbor	County Berrien
Audit Date 6/30/05	Opinion Date 2/10/06	Date Accountant Report Submitted to State: 3/21/06	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

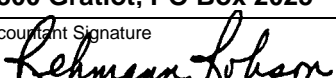
We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☒ Yes ☐ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).	✓		

Certified Public Accountant (Firm Name) Rehmann Robson			
Street Address 5800 Gratiot, PO Box 2025		City Saginaw	State MI
Accountant Signature 		ZIP 48605	Date 3/21/06



CITY OF BENTON HARBOR, MICHIGAN

Financial Statements

**For the Year Ended
June 30, 2005**



REHMANN ROBSON

Certified Public Accountants

CITY OF BENTON HARBOR, MICHIGAN
For the Year Ended June 30, 2005

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REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



INDEPENDENT AUDITORS' REPORT

February 10, 2006

Honorable Mayor and
Members of the City Commission
City of Benton Harbor, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the ***City of Benton Harbor, Michigan***, as of and for the year ended June 30, 2005, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Benton Harbor's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Twin Cities Area Transportation Authority, which represents 99% of the assets and 97% of the revenue of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose report was furnished to us, and our opinion, insofar as it relates to the amounts included for the Transportation Authority, is based solely on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Benton Harbor, Michigan, as of June 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund and enterprise zone special revenue fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 10, 2006, on our consideration of the City of Benton Harbor, Michigan's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 3-8 and the Pension System information on page 45 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Benton Harbor's basic financial statements. The combining fund financial statements and schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style.

MANAGEMENT'S DISCUSSION and ANALYSIS

City of Benton Harbor, Michigan

Management's Discussion and Analysis

The discussion and analysis of the City of Benton Harbor's financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2005. Management has prepared the financial statements and the related footnote disclosures along with the discussion and analysis. Responsibility for the completeness and fairness of this information rests with the City's management.

About the City of Benton Harbor

The City is located in Berrien County in the southwestern corner of the lower peninsula of Michigan. The City is governed by an elected nine-member commission, but operates under a manager form of government.

Because of its economically distressed status, in 1986 Benton Harbor was designated as an Enterprise Zone City by the State under the Michigan Enterprise Zone Act of 1985, and is in fact the only city in the state to receive such a designation. This designation has allowed the City to redirect certain property tax collections as well as provide incentives for tax-base growth.

Under the Act, commercial/industrial businesses located within the City limits were given certain State tax benefits in return for real and personal property investments that increased taxable value. Organizations making this investment were then assessed property taxes at one-half the state-wide average millage rate (approximately 26 mills versus total local taxes of approximately 70 mills) for 10 years. The entire tax levy (26 mills) for these "certified" properties became revenue to the City's General Fund. As the 10-year benefit period expires for these organizations, the General Fund tax revenue reverts back to the 18 operating mills approved by City voters.

The remaining commercial/industrial businesses in the City electing not to become "certified" continue to pay property taxes at voter-approved millage rates. However, the Enterprise Zone Act allows the City to recapture all local school district taxes. These taxes are reported as revenue in the Enterprise Zone Fund and restricted for capital/infrastructure expenditures to promote economic growth.

As "certified" businesses complete their 10-year certification period, General Fund revenue will decrease as indicated above. Enterprise Zone Fund revenue will increase due to the additional local school taxes recaptured on these properties.

The last commercial/industrial business certifications were approved in 1996 and the entire Enterprise Zone Act ended with property taxes levied in the City's June 30, 2005 fiscal year.

Using this Annual Report

This annual report consists of a series of financial statements. The statement of net assets and the statement of activities provide information about the activities of the City as a whole and present a longer-term view of the City's finances. This longer-term view uses the accrual basis of accounting so that it can measure the cost of providing services during the current year, and whether the taxpayers have funded the full cost of providing government services.

The Fund financial statements present a short-term view; they tell us how the taxpayers' resources were spent during the year, as well as how much is available for future spending. Fund financial statements also report the City's operations in more detail than the government-wide financial statements by providing information about the City's most significant funds. The fiduciary fund statements provide financial information about activities for which the City acts solely as a trustee or agent for the benefit of those outside of the government.

The City as a Whole

The following table shows, in a condensed format, the net assets as of the current date and compared to the prior year:

City of Benton Harbor's Net Assets

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Assets						
Current and other assets	\$ 3,388,071	\$ 2,846,575	\$ 9,632,799	\$ 9,733,441	\$ 13,020,870	\$ 12,580,016
Capital assets, net	15,635,750	12,984,809	3,330,733	3,255,087	18,966,483	16,239,896
Total assets	19,023,821	15,831,384	12,963,532	12,988,528	31,987,353	28,819,912
Liabilities						
Long-term liabilities	1,511,063	1,257,135	582,194	747,431	2,093,257	2,004,566
Other liabilities	2,131,902	1,476,142	1,337,038	832,535	3,468,940	2,308,677
Total liabilities	3,642,965	2,733,277	1,919,232	1,579,966	5,562,197	4,313,243
Net assets						
Invested in capital assets, net of related debt	15,156,763	12,774,914	3,330,733	2,536,027	18,487,496	15,310,941
Restricted	3,721,874	2,446,001	-	-	3,721,874	2,446,001
Unrestricted	(3,497,781)	(2,122,808)	7,713,567	8,872,535	4,215,786	6,749,727
Total net assets	\$ 15,380,856	\$ 13,098,107	\$ 11,044,300	\$ 11,408,562	\$ 26,425,156	\$ 24,506,669

The City's combined net assets increased 1.1 percent from a year ago - increasing from \$24,506,669 to \$26,425,156.

As we look at the governmental activities separately from the business-type activities, we can see that the net assets increased almost 1.2 percent from a year ago. The deficit in unrestricted net assets - that which can be used to finance day-to-day operations - increased by approximately \$1,375,000 for the governmental activities.

Total net assets for the business-type activities decreased a little over 3 percent while unrestricted net assets decreased approximately 13 percent.

The following table shows the changes in the net assets during the current year and as compared to the prior year:

City of Benton Harbor's Changes in Net Assets

	Governmental Activities		Business-type Activities		Total	
	2005	2004	2005	2004	2005	2004
Revenues						
Program revenues:						
Charges for services	\$ 1,087,217	\$ 1,030,753	\$ 4,037,964	\$ 3,841,195	\$ 5,125,181	\$ 4,871,948
Operating grants and contributions	2,276,232	2,117,561	-	-	2,276,232	2,117,561
Capital grants and contributions	957,101	93,101	402,495	305,098	1,359,596	398,199
General revenues:						
Property taxes	4,436,554	4,150,309	-	-	4,436,554	4,150,309
State shared revenues	2,252,769	2,273,633	-	-	2,252,769	2,273,633
Grants and contributions not restricted to specific programs	119,640	228,236	-	-	119,640	228,236
Unrestricted investment earnings	6,194	7,562	8,601	10,156	14,795	17,718
Gain on sale of capital assets	690,486	132,475	-	-	690,486	132,475
Total revenues	<u>11,826,193</u>	<u>10,033,630</u>	<u>4,449,060</u>	<u>4,156,449</u>	<u>16,275,253</u>	<u>14,190,079</u>
Expenses						
Legislative	92,311	93,115	-	-	92,311	93,115
General government	2,173,536	2,360,421	-	-	2,173,536	2,360,421
Public safety	3,844,815	3,461,988	-	-	3,844,815	3,461,988
Public works	1,452,331	1,344,931	-	-	1,452,331	1,344,931
Recreation and cultural	296,805	64,487	-	-	296,805	64,487
Community and economic development	962,798	1,460,687	-	-	962,798	1,460,687
Other governmental activities	749,275	656,426	-	-	749,275	656,426
Interest on long-term debt	8,362	9,331	-	-	8,362	9,331
Utility services	-	-	4,568,227	4,205,429	4,568,227	4,205,429
Cemetery	-	-	208,306	203,798	208,306	203,798
Total expenses	<u>9,580,233</u>	<u>9,451,386</u>	<u>4,776,533</u>	<u>4,409,227</u>	<u>14,356,766</u>	<u>13,860,613</u>
Change in net assets before transfers	2,245,960	582,244	(327,473)	(252,778)	1,918,487	329,466
Transfers	<u>36,789</u>	<u>33,036</u>	<u>(36,789)</u>	<u>(33,036)</u>	<u>-</u>	<u>-</u>
Change in net assets	2,282,749	615,280	(364,262)	(285,814)	1,918,487	329,466
Net assets, beginning of year, as restated	<u>13,098,107</u>	<u>12,482,827</u>	<u>11,408,562</u>	<u>11,694,376</u>	<u>24,506,669</u>	<u>24,177,203</u>
Net assets, end of year	<u>\$ 15,380,856</u>	<u>\$ 13,098,107</u>	<u>\$ 11,044,300</u>	<u>\$ 11,408,562</u>	<u>\$ 26,425,156</u>	<u>\$ 24,506,669</u>

Governmental Activities

The City's total governmental revenues increased by approximately \$1,793,000. The increase, which represents approximately 17.9 percent, was primarily due to increases in property taxes, grant revenue and sale of capital assets.

Expenses increased by about \$129,000 during the year. Increases resulted from higher public safety and public works costs.

Business-type Activities

The City's business-type activities consist of Utility Services as well as Cemetery operations. The City provides water to residents as well as sewage treatment services from the Benton Harbor/St. Joseph Joint Wastewater Treatment System.

Total revenues increased by \$293,000. The majority of this increase resulted from a mid-year increase in water rates charged and collected from customers. In addition, expenses increased approximately \$367,000 as the result of increases in water and sewer operating costs along with increases in salaries and healthcare expenses.

The City's Funds

Our analysis of the City's major funds begins on page 9, following the government-wide financial statements. The fund financial statements provide detail information about the most significant funds, not the City as a whole. The City Commission creates funds to help manage money for specific purposes as well as to show accountability for certain activities, such as special property tax millages. The City's major funds for 2005 include the General Fund, the Enterprise Zone Fund, and the Utility Services Fund.

The General Fund pays for most of the City's governmental services. Significant services include police and fire protection services, which incurred expenses of approximately \$4,000,000 in 2005.

The Enterprise Zone Fund pays for City-wide capital/infrastructure improvements from property tax revenue as required by the Michigan Enterprise Zone Act.

General Fund Budgetary Highlights

The City did not amend their budget during the year.

Revenue shortfalls included \$200,000 in property taxes due to the phase out of the Enterprise Zone Act, \$250,000 in shared revenue due to cutbacks by the State of Michigan and \$109,000 in sale of capital assets due to expenses related to the sale of Jean Klock Park lots. Actual Federal and State grant sources (\$199,000 and \$193,000, respectively) approximated the amount budgeted as State grant revenue only. Total General Fund revenue fell short of budgeted amounts by approximately \$582,000.

On the expenditure side, general administration costs were almost double budgeted amounts due to general liability insurance premiums, legal judgments, professional fees and capital outlay expenditures. Police Department costs exceeded budget due to the availability of additional revenue sources that allowed the department to add officers and purchase capital assets. However, some revenue will not be realized until Fiscal 2006 and some grant revenue required that the City absorb a percentage of the costs through a match. City hall and grounds costs exceeded budget due to increased compensation and professional fee expenditures. Rubbish collection fees continue to increase faster than the related revenue and exceeded budget by approximately \$98,000. Many other departments were at or below budget, which caused total General Fund expenditures to exceed budget by approximately \$855,000.

Capital Asset and Debt Administration

At the end of 2005, the City had approximately \$42,300,000 million invested in a broad range of capital assets, including buildings, police and fire equipment, water and sewer lines and streets and sidewalks. This amount included additions of \$3,700,000 during the year. In addition, the City has invested significantly in roads within the City. Infrastructure projects in process and/or completed in 2005 amounted to \$2,300,000 and are included in the additions above. Retroactive infrastructure to 1980 will be reported no later than June 30, 2007.

The City incurred additional debt in fiscal 2005 for equipment and economic development totaling \$509,681.

In 2005, the City made the final payment on all Michigan Emergency Loans. These loans, totaling \$2,440,000, were issued in 1981 through 1985 to bring some financial stability to the City. While the City still struggles financially, all loan payments were made timely. At June 30, 2005, the City retired two debt issues, freeing up approximately \$125,000 of governmental fund revenue now available for other uses.

Economic Factors and Next Year's Budgets and Rates

As discussed earlier, the final phase out of the Enterprise Zone Act at June 30, 2005 will significantly reduce General Fund and Enterprise Zone Fund tax revenue. Starting in fiscal 2006, the Enterprise Zone Fund will no longer receive property taxes and activity in this fund will be limited to using existing fund balance. The City is exploring alternate ways to fund capital/infrastructure improvements required for continued economic growth.

The economic position of the City is closely tied to that of the State. For fiscal year 2005, the State revenue sharing provided 35 percent of the City's General Fund revenues. The State continues to reduce statutory revenue sharing to all local units of government. The State's budget for its year beginning October 1, 2005 contained an agreement for the cities, villages and townships to maintain revenue sharing funding at prior year level. However, this very likely could change. The State funding problems are believed to be a multiple-year situation and future decreases may be likely.

As property tax revenue and state revenue sharing decrease, controlling General Fund expenditures becomes a significant challenge unless new revenue can be generated. The City continues to look for ways to increase its tax base to generate more property tax revenue. In fiscal 2005, twenty-plus new houses were built as part of the “Jimmy Carter Work Project” and the City was able to favorably resolve a court challenge related to the sale of a parcel of Jean Klock Park. This sale added \$600,000 to General Fund revenue in fiscal 2005. The entire parcel will be developed into 27 high-income residential lots, only three of which were sold in 2005. As lots are sold, the City is entitled to receive 75% of the sales price, which will range from \$100,000 to \$400,000 per lot. It is anticipated that lot sales will occur over the next two to three years. Construction on two more residential developments will start in late fiscal 2006. The Harbor Town subdivision will consist of 26 houses built for middle-income families and the \$20 million HOPE VI housing project will provide replacement low-income housing. As construction is completed, these properties will add significant dollars to the City’s property tax base over the next five years.

To facilitate the above projects, the City incurred significant up-front costs in fiscal 2005. This investment, which will not be returned for several years, consisted mostly of infrastructure such as replacement of water mains in the Belview/Brunson Avenue area, replacement of the Stevens Avenue sewer lift station, demolition and replacement of the North Shore Drive bridge, reconstruction/resurfacing of Colfax, Broadway and Pipestone Avenues, and recreation area improvements including Riverfront Park and a new bike path connecting points of interest throughout the City.

A major economic development effort which involves not only the City of Benton Harbor, but also the City of St. Joseph and Benton Charter Township will begin in late fiscal 2006 or early fiscal 2007. The Harbor Shores initiative will include development in the areas of water and land recreation facilities, residential housing, retail trade and arts and culture opportunities. When complete, this project could triple the City’s existing tax base over the next five years.

Contacting the City’s Management

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the City’s finances and to show the City’s accountability for the money it receives. If you have questions about this report or need additional information, we welcome you to contact the Finance Department.

BASIC FINANCIAL STATEMENTS

GOVERNMENT-WIDE FINANCIAL STATEMENTS

City of Benton Harbor, Michigan
Statement of Net Assets
June 30, 2005

	Primary Government			Component Units
	Governmental Activities	Business-type Activities	Total	
Assets				
Cash and cash equivalents	\$ (248,467)	\$ 253,800	\$ 5,333	\$ 92,953
Investments	-	312,104	312,104	-
Receivables, net	2,329,906	1,243,918	3,573,824	95,287
Internal balances	1,252,668	(1,252,668)	-	-
Prepaid items and other assets	-	87,795	87,795	26,701
Investment in joint venture	53,964	8,987,850	9,041,814	-
Capital assets not being depreciated	3,492,904	6,736	3,499,640	62,700
Capital assets being depreciated, net	12,142,846	3,323,997	15,466,843	960,985
 Total assets	 19,023,821	 12,963,532	 31,987,353	 1,238,626
Liabilities				
Accounts payable and accrued expenses	2,093,639	1,337,038	3,430,677	58,673
Long-term liabilities:				
Due within one year	616,333	245,697	862,030	-
Due in more than one year	894,730	336,497	1,231,227	-
 Total liabilities	 3,642,965	 1,919,232	 5,562,197	 58,673
Net assets				
Invested in capital assets, net of related debt	15,156,763	2,792,747	17,949,510	1,023,685
Restricted for:				
Debt service	954,028	-	954,028	-
Other purposes	2,767,846	312,104	3,079,950	-
Unrestricted (deficit)	(3,497,781)	7,939,449	4,441,668	156,268
 Total net assets	 \$ 15,380,856	 \$ 11,044,300	 \$ 26,425,156	 \$ 1,179,953

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Activities
For the Year Ended June 30, 2005

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary government				
Governmental activities:				
Legislative	\$ 92,311	\$ -	\$ -	\$ -
General government	2,173,536	303,308	-	-
Public safety	3,844,815	135,049	393,270	-
Public works	1,452,331	-	836,294	-
Recreation and cultural	296,805	-	-	-
Community and economic development	962,798	57,508	1,046,668	957,101
Other governmental activities	749,275	591,352	-	-
Interest on long-term debt	8,362	-	-	-
Total governmental activities	<u>9,580,233</u>	<u>1,087,217</u>	<u>2,276,232</u>	<u>957,101</u>
Business-type activities:				
Utility services	4,568,227	3,853,045	-	402,495
Cemetery	208,306	184,919	-	-
Total business-type activities	<u>4,776,533</u>	<u>4,037,964</u>	<u>-</u>	<u>402,495</u>
 Total primary government	 <u>\$ 14,356,766</u>	 <u>\$ 5,125,181</u>	 <u>\$ 2,276,232</u>	 <u>\$ 1,359,596</u>
Component units				
Twin Cities Area Transportation Authority	\$ 1,687,231	\$ 205,993	\$ 1,128,533	\$ 239,353
Brownfield Area Development Authority	58,939	-	6,400	-
Total component units	<u>\$ 1,746,170</u>	<u>\$ 205,993</u>	<u>\$ 1,134,933</u>	<u>\$ 239,353</u>

General revenues:

Property taxes

State shared revenues

Grants and contributions not restricted
to specific programs

Unrestricted investment earnings

Gain on sale of capital assets

Transfers - internal activities

Total general revenues and transfers

Change in net assets

Net assets, beginning of year

Net assets, end of year

The accompanying notes are an integral part of these financial statements.

Net (Expense) Revenue and Changes in Net Assets			
Primary Government			
Governmental Activities	Business-type Activities	Total	Component Units
\$ (92,311)	\$ -	\$ (92,311)	\$ -
(1,870,228)	-	(1,870,228)	-
(3,316,496)	-	(3,316,496)	-
(616,037)	-	(616,037)	-
(296,805)	-	(296,805)	-
1,098,479	-	1,098,479	-
(157,923)	-	(157,923)	-
(8,362)	-	(8,362)	-
(5,259,683)	-	(5,259,683)	-
-	(312,687)	(312,687)	-
-	(23,387)	(23,387)	-
-	(336,074)	(336,074)	-
(5,259,683)	(336,074)	(5,595,757)	-
-	-	-	(113,352)
-	-	-	(52,539)
-	-	-	(165,891)
4,436,554	-	4,436,554	128,070
2,252,769	-	2,252,769	-
119,640	-	119,640	-
6,194	8,601	14,795	739
690,486	-	690,486	5,000
36,789	(36,789)	-	-
7,542,432	(28,188)	7,514,244	133,809
2,282,749	(364,262)	1,918,487	(32,082)
13,098,107	11,408,562	24,506,669	1,212,035
\$ 15,380,856	\$ 11,044,300	\$ 26,425,156	\$ 1,179,953

FUND FINANCIAL STATEMENTS

City of Benton Harbor, Michigan
Balance Sheet
Governmental Funds
June 30, 2005

	General	Enterprise Zone	Nonmajor Funds	Totals
Assets				
Cash and cash equivalents	\$ (394,113)	\$ 123,532	\$ 22,114	\$ (248,467)
Accounts receivable	381,405	-	1,321	382,726
Notes receivable	72,407	503,012	-	575,419
Due from other governments	397,423	571,864	397,544	1,366,831
Due from other funds	1,335,635	1,314,215	1,474,438	4,124,288
Advances to other funds	522,381	409,063	653,348	1,584,792
Due from component unit	4,930	-	-	4,930
<u>TOTAL ASSETS</u>				
	\$ 2,320,068	\$ 2,921,686	\$ 2,548,765	\$ 7,790,519
<u>LIABILITIES AND FUND BALANCES</u>				
Liabilities				
Accounts payable	\$ 741,963	\$ 434,122	\$ 102,621	\$ 1,278,706
Accrued liabilities	176,444	1,271	-	177,715
Due to other governments	604,828	-	28,696	633,524
Due to other funds	2,495,583	-	494,159	2,989,742
Advances from other funds	733,718	-	732,952	1,466,670
Deferred revenue	-	541,275	167,418	708,693
Total liabilities	4,752,536	976,668	1,525,846	7,255,050
Fund balances (deficit)				
Reserved for long-term receivables	72,407	-	-	72,407
Reserved for restricted contributions	-	211,200	-	211,200
Reserved for advances	522,381	409,063	653,348	1,584,792
Unreserved:				
Undesignated (deficit)	(3,027,256)	1,324,755	-	(1,702,501)
Undesignated, reported in nonmajor:				
Special revenue funds (deficit)	-	-	(815,472)	(815,472)
Debt service funds	-	-	957,722	957,722
Permanent fund	-	-	227,321	227,321
Total fund balances (deficit)	(2,432,468)	1,945,018	1,022,919	535,469
<u>TOTAL LIABILITIES AND FUND BALANCES</u>				
	\$ 2,320,068	\$ 2,921,686	\$ 2,548,765	\$ 7,790,519

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Reconciliation of Fund Balances on the Balance Sheet
for Governmental Funds to Net Assets
of Governmental Activities on the Statement of Net Assets
June 30, 2005

Fund balances - total governmental funds	\$	535,469
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Amounts reported for *governmental activities* in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources, and therefore not reported in the funds.

Add: capital assets not being depreciated	3,492,904
Add: capital assets being depreciated	25,471,241
Subtract: accumulated depreciation	(13,328,395)

Because the focus of governmental funds is on short-term financing, some assets will not be available to pay for current-period expenditures. Those assets (such as certain receivables) are offset by deferred revenues in the governmental funds, and thus are not included in fund balance.

Add: deferred notes receivable	503,012
Add: deferred grants receivable	167,418

The government's investment in its joint venture is not a financial resource, and therefore not reported in the funds.

Add: investment in joint venture	53,964
----------------------------------	--------

Certain liabilities, such as bonds payable, are not due and payable in the current period, and therefore are not reported in the funds.

Subtract: loans and leases payable	(1,178,987)
Subtract: compensated absences	(332,076)
Subtract: accrued interest on long-term liabilities	(3,694)

Net assets of governmental activities	\$	<u>15,380,856</u>
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The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2005

	General	Enterprise Zone	Nonmajor Funds	Totals
Revenue				
Taxes and special assessments	\$ 2,379,633	\$ 1,705,370	\$ 581,551	\$ 4,666,554
Federal sources	180,330	-	842,940	1,023,270
State sources	2,465,709	924,101	836,294	4,226,104
Licenses and permits	56,481	-	-	56,481
Fines and forfeits	83,881	-	-	83,881
Charges for services	870,845	109,186	-	980,031
Contributions	-	69,310	-	69,310
Interest	3,849	-	735	4,584
Other revenue	313,142	1,610	-	314,752
Total revenue	6,353,870	2,809,577	2,261,520	11,424,967
Expenditures				
Current:				
Legislative	92,311	-	-	92,311
General government	2,748,520	-	-	2,748,520
Public safety	3,987,473	-	-	3,987,473
Public works	410,243	-	825,170	1,235,413
Recreation and cultural	220,252	-	-	220,252
Community and economic development	139,991	2,386,046	1,043,776	3,569,813
Other	749,275	150,000	-	899,275
Debt service:				
Principal	90,589	100,000	101,286	291,875
Interest	3,580	-	6,630	10,210
Total expenditures	8,442,234	2,636,046	1,976,862	13,055,142
Revenue over (under) expenditures	(2,088,364)	173,531	284,658	(1,630,175)
Other financing sources (uses)				
Proceeds from long-term debt	359,681	150,000	-	509,681
Sale of capital assets	690,486	-	-	690,486
Transfers in	76,891	50,000	119,720	246,611
Transfers (out)	-	(90,102)	(119,720)	(209,822)
Total other financing sources (uses)	1,127,058	109,898	-	1,236,956
Net change in fund balances	(961,306)	283,429	284,658	(393,219)
Fund balances (deficit), beginning of year	(1,471,162)	1,661,589	738,261	928,688
Fund balances (deficit), end of year	\$ (2,432,468)	\$ 1,945,018	\$ 1,022,919	\$ 535,469

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Reconciliation of the Statement of Revenue, Expenditures
and Changes in Fund Balances
of Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2005

Net change in fund balances - total governmental funds	\$ (393,219)
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Amounts reported for *governmental activities* in the statement of activities are different because:

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Add: capital outlay	3,324,644
Subtract: depreciation expense	(673,703)

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds, but rather are deferred to the following fiscal year.

Subtract: collections on notes receivable	(51,678)
Add: new loans made on notes receivable	150,000
Add: grants receivable collected more than 60 days after year end	167,418

The government's investment in its joint venture is not a financial resource, and therefore not reported in the funds.

Add: increase in value of investment in joint venture	11,367
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Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long term-liabilities.

Add: principal payments on long-term liabilities	291,875
Subtract: loan and lease proceeds received	(509,681)

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.

Add: change in accrued interest on bonds	1,848
Subtract: increase in the accrual of compensated absences	(36,122)

Change in net assets of governmental activities	\$ <u>2,282,749</u>
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The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund
For the Year Ended June 30, 2005

	Original/ Final Budget	Actual	Actual over (under) Final Budget
Revenue			
Taxes			
Real and personal property taxes	\$ 2,025,000	\$ 1,756,063	\$ (268,937)
Delinquent taxes	210,000	265,356	55,356
Payments in lieu of taxes	400,000	298,922	(101,078)
Other taxes	50,000	59,292	9,292
Total taxes	2,685,000	2,379,633	(305,367)
Federal sources	-	180,330	180,330
State sources			
State shared revenue	2,505,000	2,252,769	(252,231)
State grants	397,000	212,940	(184,060)
Total state sources	2,902,000	2,465,709	(436,291)
Licenses and permits	78,000	56,481	(21,519)
Fines and forfeits	40,000	83,881	43,881
Charges for services			
Cable franchise fees	42,000	36,118	(5,882)
Rubbish fees	546,600	591,352	44,752
Registration fees	75,000	68,375	(6,625)
Administrative fees	175,000	175,000	-
Total charges for services	838,600	870,845	32,245
Interest	50,000	3,849	(46,151)
Other revenue			
Rental income	157,000	193,502	36,502
Reimbursements	32,000	64,487	32,487
Miscellaneous	153,000	55,153	(97,847)
Total interest and rentals	342,000	313,142	(28,858)
Total revenue	6,935,600	6,353,870	(581,730)

continued...

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund (Continued)
For the Year Ended June 30, 2005

	Original/ Final Budget	Actual	Actual over (under) Final Budget
Expenditures			
Legislative			
Mayor / Commission	\$ 135,050	\$ 92,311	\$ (42,739)
General government			
City Manager	188,100	158,157	(29,943)
City Assessor	213,182	186,474	(26,708)
City Attorney	170,000	238,025	68,025
City Clerk	194,600	145,807	(48,793)
Elections	44,700	39,414	(5,286)
Personnel department	123,820	107,281	(16,539)
Finance department	309,625	291,670	(17,955)
Purchasing / risk management	-	244	244
City hall and grounds	289,875	393,910	104,035
General administration	645,500	1,187,538	542,038
Total general government	2,179,402	2,748,520	569,118
Public safety			
Police	2,011,539	2,505,425	493,886
Police general employees	604,072	330,268	(273,804)
Fire	1,096,214	1,009,482	(86,732)
Inspection department	238,723	142,298	(96,425)
Total public safety	3,950,548	3,987,473	36,925
Public works			
City Engineer	-	(2,291)	(2,291)
Public works administration	213,862	191,492	(22,370)
Public works stabilization	5,800	1,339	(4,461)
Streets and lighting	234,500	219,703	(14,797)
Total public works	454,162	410,243	(43,919)
Recreation and cultural			
Parks department	-	76,243	76,243
Armory	25,000	96,817	71,817
Recreation	-	47,192	47,192
Total recreation and cultural	25,000	220,252	195,252

continued...

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund (Concluded)
For the Year Ended June 30, 2005

	Original/ Final Budget	Actual	Actual over (under) Final Budget
Expenditures (concluded)			
Community and economic development			
Economic development	\$ 98,082	\$ 139,991	\$ 41,909
Other expenditures			
Rubbish collection	550,000	648,370	98,370
Aid to other agencies	119,500	100,905	(18,595)
Total other expenditures	669,500	749,275	79,775
Debt service			
Principal	75,000	90,589	15,589
Interest	-	3,580	3,580
Total debt service	75,000	94,169	19,169
Total expenditures	7,586,744	8,442,234	855,490
Revenue over (under) expenditures	(651,144)	(2,088,364)	(1,437,220)
Other financing sources (uses)			
Loan proceeds	45,000	359,681	314,681
Sale of capital assets	800,000	690,486	(109,514)
Transfers in	-	76,891	76,891
Total other financing sources (uses)	845,000	1,127,058	282,058
Net change in fund balances	193,856	(961,306)	(1,155,162)
Fund balance (deficit), beginning of year	(1,471,162)	(1,471,162)	-
Fund balance (deficit), end of year	\$ (1,277,306)	\$ (2,432,468)	\$ (1,155,162)

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenditures and Changes in Fund Balance
Budget and Actual - Enterprise Zone
For the Year Ended June 30, 2005

	Original Budget	Final Budget	Actual	Actual over (under) Final Budget
Revenue				
Taxes	\$ 1,000,000	\$ 1,000,000	\$ 1,705,370	\$ 705,370
State sources	603,113	603,113	924,101	320,988
Charges for services	-	-	109,186	109,186
Contributions	-	56,509	69,310	12,801
Interest	-	-	1,610	1,610
Total revenue	1,603,113	1,659,622	2,809,577	1,149,955
Expenditures				
Community and economic development:				
City development	1,548,113	1,604,622	2,285,886	681,264
Administration	55,000	55,000	100,160	45,160
Other:				
Aid to other agencies	-	-	150,000	150,000
Debt service:				
Principal	-	-	100,000	100,000
Total expenditures	1,603,113	1,659,622	2,636,046	976,424
Revenue over expenditures	-	-	173,531	173,531
Other financing sources				
Loan proceeds	-	-	150,000	150,000
Transfers in	-	-	50,000	50,000
Transfers out	-	-	(90,102)	(90,102)
Total other financing sources	-	-	109,898	109,898
Net changes in fund balances	-	-	283,429	283,429
Fund balances, beginning of year	1,661,589	1,661,589	1,661,589	-
Fund balances end of year	\$ 1,661,589	\$ 1,661,589	\$ 1,945,018	\$ 283,429

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Net Assets
Proprietary Funds
June 30, 2005

	Utility Services	Cemetery (Nonmajor)	Totals
Assets			
Current assets:			
Cash and cash equivalents	\$ 244,772	\$ 9,028	\$ 253,800
Accounts receivable	1,197,615	101	1,197,716
Due from other governments	46,202	-	46,202
Due from other funds	34,758	-	34,758
Inventory	-	69,145	69,145
Total current assets	<u>1,523,347</u>	<u>78,274</u>	<u>1,601,621</u>
Noncurrent assets:			
Restricted investments	-	312,104	312,104
Investment in joint venture	8,987,850	-	8,987,850
Bond issuance costs	18,650	-	18,650
Capital assets not being depreciated	6,626	110	6,736
Capital assets being depreciated, net	3,289,569	34,428	3,323,997
Total noncurrent assets	<u>12,302,695</u>	<u>346,642</u>	<u>12,649,337</u>
Total assets	<u>13,826,042</u>	<u>424,916</u>	<u>14,250,958</u>
Liabilities			
Current liabilities:			
Accounts payable	537,527	3,097	540,624
Accrued liabilities	123,139	3,759	126,898
Due to other governments	669,516	-	669,516
Due to other funds	1,134,546	34,758	1,169,304
Advances from other funds	-	118,122	118,122
Current portion of long-term debt	229,967	15,730	245,697
Total current liabilities	<u>2,694,695</u>	<u>175,466</u>	<u>2,870,161</u>
Long-term liabilities:			
Due in more than one year	311,952	24,545	336,497
Total liabilities	<u>3,006,647</u>	<u>200,011</u>	<u>3,206,658</u>
Net assets			
Invested in capital assets, net of related debt	2,778,775	13,972	2,792,747
Restricted	-	312,104	312,104
Unrestricted (deficit)	8,040,620	(101,171)	7,939,449
Total net assets	<u>\$ 10,819,395</u>	<u>\$ 224,905</u>	<u>\$ 11,044,300</u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Revenue, Expenses
and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended June 30, 2005

	Utility Services	Cemetery (Nonmajor)	Totals
Operating revenue			
Charges for services:			
Water sales	\$ 2,349,846	\$ -	\$ 2,349,846
Sewer sales	1,152,622	-	1,152,622
Other	350,577	184,919	535,496
Total operating revenue	3,853,045	184,919	4,037,964
Operating expense			
Cost of services:			
Water	2,957,086	-	2,957,086
Sewer	772,137	-	772,137
Cemetery	-	183,460	183,460
Administrative costs	531,815	-	531,815
Depreciation	263,436	22,520	285,956
Total operating expense	4,524,474	205,980	4,730,454
Operating income (loss)	(671,429)	(21,061)	(692,490)
Non-operating revenue (expenses)			
Interest income	2,208	6,393	8,601
Income from joint venture	402,495	-	402,495
Interest expense	(30,313)	(2,326)	(32,639)
Amortization of bond issuance costs	(13,440)	-	(13,440)
Total non-operating revenue (expenses)	360,950	4,067	365,017
Income (loss) before transfers	(310,479)	(16,994)	(327,473)
Transfers in (out)			
Transfers in	27,120	-	27,120
Transfers (out)	(63,909)	-	(63,909)
Change in net assets	(347,268)	(16,994)	(364,262)
Net assets, beginning of year	11,166,663	241,899	11,408,562
Net assets, end of year	<u>\$ 10,819,395</u>	<u>\$ 224,905</u>	<u>\$ 11,044,300</u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Cash Flows
Proprietary Funds
For the Year Ended June 30, 2005

	Utility Services	Cemetery (Nonmajor)	Totals
Cash flows from operating activities			
Cash received from customers	\$ 3,958,644	\$ 188,968	\$ 4,147,612
Cash payments to suppliers for goods and services	(2,074,680)	(82,131)	(2,156,811)
Cash payments to employees for services	(1,343,891)	(142,496)	(1,486,387)
Net cash provided by (used in) operating activities	540,073	(35,659)	504,414
Cash flows from non-capital financing activities			
Transfers in from other funds	27,120	-	27,120
Transfers out to other funds	(63,909)	-	(63,909)
Net cash used in non-capital financing activities	(36,789)	-	(36,789)
Cash flows from capital and related financing activities			
Purchase of capital assets	(361,601)	-	(361,601)
Interest payments	(30,313)	(2,326)	(32,639)
Principal payments	(170,768)	(10,306)	(181,074)
Net cash used in capital and related financing activities	(562,682)	(12,632)	(575,314)
Cash flows from investing activities			
Interest income	2,208	183	2,391
Net increase (decrease) in cash and cash equivalents	(57,190)	(48,108)	(105,298)
Cash and cash equivalents, beginning of year	301,963	57,136	359,099
Cash and cash equivalents, end of year	<u>\$ 244,773</u>	<u>\$ 9,028</u>	<u>\$ 253,801</u>

continued...

City of Benton Harbor, Michigan
Statement of Cash Flows
Proprietary Funds (Concluded)
For the Year Ended June 30, 2005

	Utility Services	Cemetery (Nonmajor)	Totals
Cash flows from operating activities			
Operating income (loss)	\$ (671,429)	\$ (21,061)	\$ (692,490)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:			
Depreciation	263,436	22,520	285,956
Changes in assets and liabilities:			
Accounts receivable	(564,176)	1,650	(562,526)
Due from other governments	498,410	-	498,410
Due from other funds	171,365	2,399	173,764
Accounts payable	304,504	(11,849)	292,655
Accrued liabilities	24,583	3,759	28,342
Due to other governments	183,507	-	183,507
Due to other funds	324,218	-	324,218
Advances from other funds	-	(36,401)	(36,401)
Compensated absences	5,655	3,324	8,979
Net cash provided by operating activities	<u>\$ 540,073</u>	<u>\$ (35,659)</u>	<u>\$ 504,414</u>

Non-cash transactions

There were no significant non-cash transactions during the fiscal year.

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Fiduciary Net Assets
Fiduciary Funds
June 30, 2005

	<u>Pension Trust Funds</u>
Assets	
Cash and cash equivalents	\$ 71,292
Investments:	
Fixed income securities	5,551,824
Equities	9,613,220
Money market	525,855
Receivables:	
Accrued interest	35,398
Other	<u>557,215</u>
Total assets	16,354,804
 Liabilities	
Due to resigned employees	<u>60,887</u>
 Net Assets	
Held in trust for pension benefits and other purposes	<u><u>\$ 16,293,917</u></u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Statement of Changes in Fiduciary Net Assets
Fiduciary Funds
For the Year Ended June 30, 2005

	<u>Pension Trust Funds</u>
Additions	
Taxes	\$ 258,063
Contributions:	
Employer	340,261
Employee	194,472
Total contributions	<u>534,733</u>
Investment earnings:	
Net appreciation in fair value of investments	549,681
Interest and dividends	604,375
Net investment earnings	<u>1,154,056</u>
Total additions	<u>1,946,852</u>
Deductions	
Pension benefits paid directly to participants	1,168,855
Administrative expenses	<u>205,238</u>
Total deductions	<u>1,374,093</u>
Change in net assets	572,759
Net assets, beginning of year	<u>15,721,158</u>
Net assets, end of year	<u><u>\$ 16,293,917</u></u>

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Combining Statement of Net Assets
Component Units
June 30, 2005

	Transportation Authority	Brownfield Redevelopment Authority	Total
Assets			
Cash and cash equivalents	\$ 92,953	\$ -	\$ 92,953
Receivables, net	88,887	-	88,887
Due to other governments	-	6,400	6,400
Prepaid items and other assets	26,701	-	26,701
Capital assets not being depreciated	62,700	-	62,700
Capital assets being depreciated, net	960,985	-	960,985
Total assets	1,232,226	6,400	1,238,626
Liabilities			
Account payable and accrued liabilities	47,115	6,628	53,743
Due to primary government	-	4,930	4,930
Total liabilities	47,115	11,558	58,673
Net assets			
Invested in capital assets	1,023,685	-	1,023,685
Unrestricted (deficit)	161,426	(5,158)	156,268
Total net assets	\$ 1,185,111	\$ (5,158)	\$ 1,179,953

The accompanying notes are an integral part of these financial statements.

City of Benton Harbor, Michigan
Combining Statement of Activities
Component Units
For the Year Ended June 30, 2005

	Transportation Authority	Brownfield Redevelopment Authority	Total
Expenses	\$ 1,687,231	\$ 58,939	\$ 1,746,170
Program revenues			
Charges for services	205,993	-	205,993
Operating grants and contributions	1,128,533	6,400	1,134,933
Capital grants and contributions	239,353	-	239,353
Total program revenues	1,573,879	6,400	1,580,279
Net (expense) revenue	(113,352)	(52,539)	(165,891)
General revenues:			
Property taxes	80,689	47,381	128,070
Unrestricted investment earnings	739	-	739
Gain on sale of capital assets	5,000	-	5,000
Total general revenues	86,428	47,381	133,809
Change in net assets	(26,924)	(5,158)	(32,082)
Net assets, beginning of year	1,212,035	-	1,212,035
Net assets (deficit), end of year	\$ 1,185,111	\$ (5,158)	\$ 1,179,953

The accompanying notes are an integral part of these financial statements.

NOTES to the FINANCIAL STATEMENTS

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the City of Benton Harbor (the “City”) conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the City of Benton Harbor.

Reporting Entity

The City of Benton Harbor is governed by an elected nine-member commission. The accompanying financial statements present the City and its component units, entities for which the City is considered to be financially accountable. Although blended component units are legal separate entities, in substance, they are part of the City’s operations. Each discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City (*see discussion below for description*).

Blended Component Unit – The City of Benton Harbor blends one component unit, the Economic Development Corporation (the “Corporation”). The Corporation was established to encourage the location and expansion of industrial/commercial enterprises with the City limits on the City’s behalf. The City provides all administrative functions of the Corporation and appoints two commission members to the Corporation’s nine-member board. The Economic Development Corporation has been blended with the City’s special revenue funds and is considered a non-major fund.

Discretely Presented Component Unit – The City discretely presents two component unit in these financial statements, the Twin Cities Area Transportation Authority, and the Brownfield Redevelopment Authority.

The Transportation Authority was incorporated in the State of Michigan on July 1, 1974 under Public Act 55 of 1963. The purpose of the Authority is to acquire, own, operate, and manage a public transportation system within the boundaries of the City of Benton Harbor, its only participating municipality. Given that the City has significant influence over the Authority and is the only participating municipality, the Twin Cities Area Transportation Authority is a component unit of the City of Benton Harbor. The Twin Cities Area Transportation Authority uses enterprise fund accounting. A complete financial report can be obtained from the Twin Cities Area Transportation Authority at 275 East Wall Street, Benton Harbor, MI 49023-0837, Telephone (269) 927-2268.

The Brownfield Redevelopment Authority was established pursuant to Act 381 of the Public Acts of 1996, as amended. The purpose of the Authority is to treat and revitalize environmentally distressed brownfield zones. The Authority’s budget is subject to approval by the City Commission.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Jointly Governed Organizations

Southwest Michigan Regional Airport Authority – In fiscal 1998, four municipalities approved the establishment of an Airport Authority to oversee airport operations. Operations are partially funded by property taxes. In late July 1998, control of airport operations was transferred to the Authority. The Authority is governed by a board of four members, including one from each participating municipality. On dissolution, net assets will be shared on a prorata basis based on amounts contributed to the Authority. The City's equity share was 4.9 percent at June 30, 2005. Based on audited financial statements, an equity interest has been recorded in the City's basic financial statements as a governmental activity.

Benton Harbor-St. Joseph Joint Sewage Disposal Plant – The City is a participant with the City of St. Joseph in a joint venture to provide sanitary sewage treatment and collection facilities for the residents of these communities. The Benton Harbor-St. Joseph Joint Wastewater Treatment Plant was created for that purpose. Upon dissolution of the Plant, the net assets will be shared on an equal basis with the City of St. Joseph. The Plant is governed by a board of eight members consisting of three members each from Benton Harbor and St. Joseph and two members chosen from neighboring communities. The City's net investment and its share of the operating results of the Plant are reported in the City's Utility Services Fund (a business type activity).

"Corridor" Corporation – The City of Benton Harbor formed a development corporation with Cornerstone Alliance, a nonprofit organization established to promote economic growth in Benton Harbor and surrounding communities. The intent of this organization is to promote economic development in the "Benton Harbor Airport Corridor". The entity is owned 50 percent by the City and 50 percent by Cornerstone. The City contributed City owned property to the corporation. Cornerstone Alliance has incurred expenses on behalf of this corporation totaling \$117,650. These amounts are reflected as accounts receivable on Cornerstone's records, repayment which is dependent on future development of property held by "Corridor" Corporation. The only significant activity in the "Corridor" Corporation to date is the contribution of the property. In the future, when development activity begins, this investment will be accounted for on the equity method.

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include: (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenue.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

Property taxes, state-shared revenue, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period. All other revenue items are considered to be available only when cash is received by the City.

The City reports the following major governmental funds:

The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The Enterprise Zone Fund is a special revenue fund that accounts for property taxes provided by the Michigan Enterprise Zone Act that are restricted for capital/infrastructure improvements.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

The City reports the following major proprietary fund:

The Utility Services Fund accounts for the activities of the City's water distribution and wastewater treatment systems.

Additionally, the City reports the following fund types:

Special revenue funds. These funds account for revenue sources that are legally restricted to expenditures for specific purposes not including capital projects or permanent funds.

Debt service funds. These funds account for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

Permanent fund. This fund accounts for resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support specified government programs.

Pension trust funds. These funds account for the activities of both the General Employees and Police and Fire Employees' retirement systems, which accumulate resources for pension benefit payments to qualified employees.

Private sector standards of accounting issued prior to December 1, 1989 are generally followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with the standards of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private sector standards.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City's water/sewer function and various other functions of the City. Eliminations of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenue include: (1) charges to customers or applicants for goods, services, or privileges provided; (2) operating grants and contributions; and (3) capital grants and contributions. Internally dedicated resources are reported as general revenue rather than as program revenue. Likewise, general revenue includes all taxes.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenue of our proprietary funds relates to charges to customers for sales and services. The Utility Services Fund also recognizes the portion of tap fees intended to recover current costs (e.g., labor and materials to hook up new customers) as operating revenue. Operating expenses for proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Assets, Liabilities, and Net Assets or Equity

Bank Deposits and Investments – Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired. Investments are stated at fair value.

State statutes authorize the government to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations, and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

Investments are stated at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. Investments that do not have established market values are reported at estimated fair value. Cash deposits are reported at carrying amounts, which reasonably approximates fair value.

Unrealized appreciation or depreciation on pension trust fund investments due to changes in fair value are recognized each year.

Receivables and Payables – In general, outstanding balances between funds are reported as “due to/from other funds.” Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as “advances to/from other funds.” Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as “internal balances.”

All trade and property tax receivables are shown as net of allowance for uncollectible amounts. Property taxes are levied on each July 1 on the taxable valuation of property as of the preceding December 31. Taxes are considered delinquent on July 1 of the following year, at which time penalties and interest are assessed.

Inventories and Prepaid Items – Inventories are valued at cost, on a first-in, first-out basis. Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items in both government-wide and fund financial statements.

Capital Assets – Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the City as assets with an initial individual cost of more than \$1,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Capital assets are depreciated using the straight-line method over the following useful lives:

Roads and sidewalks	10 to 15 years
Land improvements	5 to 75 years
Buildings and building improvements	10 to 30 years
Water and sewer distribution systems	12 to 75 years
Vehicles	5 years
Computer equipment	5 years
Office equipment	7 years
Office furnishings	7 years
Other tools and equipment	7 years

Infrastructure has only been recorded for projects that occurred subsequent to June 30, 2002. Retroactive infrastructure to 1980 will be reported prior to June 30, 2007.

Compensated Absences (Vacation and Sick Leave) – It is the City’s policy to permit employees to accumulate earned but unused sick and vacation pay benefits. There is no liability for unpaid accumulated sick leave except for amounts accumulated by police and fire employees. Vacation pay for all employees and sick pay for police and fire employees is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for these amounts is reported in governmental funds only for employee terminations as of year end.

Long-term Obligations – In the government-wide financial statements and the proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund-type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt. In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses. Issuance costs are reported as debt service expenditures.

Fund Equity – In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose.

2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information – Annual budgets are adopted on a basis consistent with generally accepted accounting principles for the General Fund and all Special Revenue Funds except the Federal and State Grant funds, which are budgeted on a project-length-basis. The annual budget is prepared by the City management and adopted by the City Commission; subsequent amendments are approved by the City Commission. All annual appropriations lapse at fiscal year end and encumbrances are not included as expenditures. During the year, the budget was amended in a legally permissible manner.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

The budget document presents information by fund, function, department, and line items. The legal level of budgetary control adopted by the governing body is the department level. Expenditure budget overruns are as reported in the statement of revenue, expenditures, and changes in fund balance – budget and actual for the General Fund and Enterprise Zone Fund.

Fund Deficits – The City has accumulated unreserved fund deficits in the following individual funds:

<u>Fund</u>	<u>Balance</u>
General Fund	\$(3,027,256)
Special Revenue Funds:	
Major Streets Fund	(57,841)
Local Streets Fund	(314,111)
Federal Grants Fund	(377,499)
State Grants Fund	(66,021)
Enterprise Fund – Cemetery Fund	(121,737)
Component Unit:	
Brownfield Redevelopment Authority	(5,158)

Deficit Plan

The City of Benton Harbor General Fund has a total deficit fund balance of \$2,432,468 for the year ended June 30, 2005 and has structured a five-year plan to reduce this deficit. This deficit reduction was included in the City's budget beginning in fiscal year 2005, and will continue to be until the deficit is eliminated. Overall, the plan will seek to increase revenues and reduce costs while maintaining service levels. In addition, the City is looking at a reduction in normal expenditures by management controls and restructuring processes and procedures. The City hopes to achieve this through improved rubbish collections, land sales of beach-front property, sales of tax-reverted property, and property reassessments. The City looks to control expenditures through management/departmental oversight of cell phone usage and gasoline consumption, as well as other general costs.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

3. DEPOSITS AND INVESTMENTS

Following is a reconciliation of deposit and investment balances as of June 30, 2005:

Statement of Net Assets

Cash and cash equivalents – primary government	\$ 5,333
Cash and cash equivalents – component units	92,953
Investments	312,104

Statement of Fiduciary Net Assets

Cash and cash equivalents	71,292
Investments	<u>15,690,899</u>

Total **\$ 16,172,581**

Deposits and Investments:

Bank deposits:	
Checking/savings accounts	\$ 167,898
Certificates of deposit (due within one year)	312,104
Investments in securities and mutual funds:	
Mutual and cash management funds	
(uncategorized as to risk)	8,195,216
US Government agencies (GNMA)	1,318
Common stock (domestic corporations)	6,865,488
Foreign equities (international corporations)	628,877
Cash on hand	<u>1,680</u>

Total **\$ 16,172,581**

The City chooses to disclose its investments by specifically identifying each, as shown above. The City's investment in US Government securities (GNMA) are rated AAA and are backed by the full faith and credit of the United States. The mutual and cash management funds do not have credit ratings.

Interest Rate Risk. State law limits the allowable investments and the maturities of some of the allowable investments as identified in the summary of significant accounting policies. The City's investment policy does not have specific limits in excess of state law on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk. State law limits investments to specific government securities, certificates of deposits and bank accounts with qualified financial institutions, commercial paper with specific maximum maturities and ratings when purchased, bankers acceptances of specific financial institutions, qualified mutual funds and qualified external investment pools as identified in the list of authorized investments in the summary of significant accounting policies. The City's investment policy does not have specific limits in excess of state law on investment credit risk. Credit risk ratings, where applicable, have been identified above for the City's investments.

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a bank failure, the City's deposits may not be returned. State law does not require and the City does not have a policy for deposit custodial credit risk. As of year end, \$959,681 of the City's bank balance of \$1,203,107 was exposed to custodial credit risk because it was uninsured and uncollateralized.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

The City's investment policy does not specifically address this risk, although the City believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the City evaluates each financial institution with which it deposits City funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Custodial Credit Risk – Investments. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State law does not require and the City does not have a policy for investment custodial credit risk. On the investments listed above, there is no custodial credit risk, as these investments are uncategorized as to credit risk.

Concentration of Credit Risk. State law limits allowable investments but does not limit concentration of credit risk as identified in the list of authorized investments in the summary of significant accounting policies. The City's investment policy does not have specific limits in excess of state law on concentration of credit risk. All investments held at year end are reported above.

4. RECEIVABLES

Receivables as of year end, including the applicable allowances for uncollectible accounts, are as follows:

	Governmental Activities	Business-Type Activities	Component Units
Taxes	\$ 1,742,376	\$ -	\$ -
Accounts	592,726	2,729,202	88,887
Due from other governments	1,366,831	46,202	6,400
Due from component units	4,930	-	-
Notes	575,419	-	-
Less: Allowance for uncollectibles	(1,952,376)	(1,531,486)	-
Total	\$ 2,329,906	\$ 1,243,918	\$ 95,287
Due in more than one year	\$ 472,000	\$ -	\$ -

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

5. CAPITAL ASSETS

Capital asset activity of the City's governmental and business-type activities was as follows:

	Beginning Balance	Additions	Disposals	Ending Balance
Governmental Activities				
Capital assets, not being depreciated:				
Land	\$ 1,429,841	\$ 130,155	\$ -	\$ 1,559,996
Airport land	1,932,908	-	-	1,932,908
Total capital assets not being depreciated	3,362,749	130,155	-	3,492,904
Capital assets, being depreciated:				
Roads and sidewalks	1,933,847	2,257,951	-	4,191,798
Airport depreciable property	9,112,065	-	-	9,112,065
Land improvements	382,314	169,930	-	552,244
Buildings and improvements	6,421,723	24,781	-	6,446,504
Vehicles	1,763,740	179,927	-	1,943,667
Computer equipment	456,437	170,694	-	627,131
Office equipment	299,778	201,950	-	501,728
Office furnishings	194,269	-	-	194,269
Other tools and equipment	1,712,579	189,256	-	1,901,835
Total capital assets being depreciated	22,276,752	3,194,489	-	25,471,241
Less accumulated depreciation for:				
Roads and sidewalks	(180,558)	(156,954)	-	(337,512)
Airport depreciable property	(6,278,616)	-	-	(6,278,616)
Land improvements	(321,095)	(6,608)	-	(327,703)
Buildings and improvements	(2,065,585)	(246,910)	-	(2,312,495)
Vehicles	(1,636,570)	(106,154)	-	(1,742,724)
Computer equipment	(437,859)	(24,489)	-	(462,348)
Office equipment	(164,652)	(29,620)	-	(194,272)
Office furnishings	(183,061)	(2,491)	-	(185,552)
Other tools and equipment	(1,386,696)	(100,477)	-	(1,487,173)
Total accumulated depreciation	(12,654,692)	(673,703)	-	(13,328,395)
Total capital assets being depreciated, net	9,622,060	2,520,786	-	12,142,846
Capital assets, net	\$ 12,984,809	\$ 2,650,941	\$ -	\$ 15,635,750

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

	Beginning Balance	Additions	Disposals	Ending Balance
Business-type Activities				
Capital assets, not being depreciated:				
Land	\$ 6,736	\$ -	\$ -	\$ 6,736
Total capital assets not being depreciated	<u>6,736</u>	<u>-</u>	<u>-</u>	<u>6,736</u>
Capital assets, being depreciated:				
Water and sewer distribution systems	8,019,712	276,107	-	8,295,819
Land improvements	68,285	-	-	68,285
Buildings and building improvements	2,330,995	17,588	-	2,348,583
Vehicles	318,918	57,784	-	376,702
Other tools and equipment	2,187,029	10,123	-	2,197,152
Total capital assets being depreciated	<u>12,924,939</u>	<u>361,602</u>	<u>-</u>	<u>13,286,541</u>
Less accumulated depreciation for:				
Water and sewer distribution systems	(6,058,024)	(161,683)	-	(6,219,707)
Land improvements	(66,720)	(84)	-	(66,804)
Buildings and building improvements	(1,389,974)	(13,117)	-	(1,403,091)
Vehicles	(300,039)	(24,029)	-	(324,068)
Other tools and equipment	(1,861,831)	(87,043)	-	(1,948,874)
Total accumulated depreciation	<u>(9,676,588)</u>	<u>(285,956)</u>	<u>-</u>	<u>(9,962,544)</u>
Total capital assets being depreciated, net	<u>3,248,351</u>	<u>75,646</u>	<u>-</u>	<u>3,323,997</u>
Capital assets, net	<u><u>\$ 3,255,087</u></u>	<u><u>\$ 75,646</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 3,330,733</u></u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Depreciation expense was charged to programs of the primary government as follows:

Governmental Activities:

General government	\$ 140,123
Public safety	123,188
Public works	220,177
Recreation and cultural	75,684
Community and economic development	<u>114,531</u>

Total governmental activities	<u>\$ 673,703</u>
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Business-type Activities:

Utility services	\$ 263,436
Cemetery	<u>22,520</u>

Total business-type activities	<u>\$ 285,956</u>
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6. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses as of year end are as follows:

	Governmental Activities	Business-Type Activities	Component Units
Accounts payable	\$ 1,278,706	\$ 540,624	\$ 53,743
Due to other governments	604,828	669,516	-
Accrued liabilities	210,105	126,898	-
Due to primary government	<u>-</u>	<u>-</u>	<u>4,930</u>
Total	<u>\$ 2,093,639</u>	<u>\$ 1,337,038</u>	<u>\$ 58,673</u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

7. INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS

The composition of interfund balances is as follows:

	Due from				Total
	General Fund	Nonmajor Governmental	Utility Services	Cemetery	
Due to					
General Fund	\$ -	\$ 489,786	\$ 845,849	\$ -	\$ 1,335,635
Enterprise Zone Fund	1,312,721	1,494	-	-	1,314,215
Nonmajor governmental funds	1,182,862	2,879	288,697	-	1,474,438
Utility Services Fund	-	-	-	34,758	34,758
	<u>\$ 2,495,583</u>	<u>\$ 494,159</u>	<u>\$ 1,134,546</u>	<u>\$ 34,758</u>	<u>\$ 4,159,046</u>

	Advance to			Total
	General Fund	Enterprise Zone	Nonmajor Governmental	
Advance from				
General Fund	\$ -	\$ 409,063	\$ 324,655	\$ 733,718
Nonmajor governmental funds	404,259	-	328,693	732,952
Cemetery Fund	118,122	-	-	118,122
	<u>\$ 522,381</u>	<u>\$ 409,063</u>	<u>\$ 653,348</u>	<u>\$ 1,584,792</u>

Interfund receivables are the result of timing differences in the transfer of funds to cover expenditures from shared bank accounts and grants funds where draws were received subsequent to year when expenditures occurred. Interfund receivables not expected to be repaid within one year are classified as advances.

Fund Providing Resources	Fund Receiving Resources	Amount
Enterprise Zone Fund	General Fund	\$ 62,982
Enterprise Zone Fund	Utility Services Fund	27,120
Major Street Fund	Local Street Fund	119,720
Utility Services Fund	General Fund	13,909
Utility Services Fund	Enterprise Zone Fund	50,000
Total Transfers		<u><u>\$ 273,731</u></u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Interfund transfers are the result of payment for services, use of City facilities by the other funds of the City, or to transfer resources from the fund that is required to receive them to the fund that is required or allowed to spend them.

8. LONG-TERM DEBT

The City issues bonds to provide for the acquisition and construction of major capital facilities. General obligation bonds are direct obligations and pledge the full faith and credit of the City. County contractual agreements and installment purchase agreements are also general obligations of the government.

	Issuance Date	Interest Rates	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
General obligation bonds							
<i>Business-type Activities:</i>							
1997 Water bonds	12/1/1997	4.3%-4.375%	\$ 685,000	\$ -	\$ 170,000	\$ 515,000	\$ 180,000

Annual debt service requirements to maturity for General obligation bonds are as follows:

Years Ending December 31	Business-Type Activities	
	Principal	Interest
2006	\$ 180,000	\$ 22,532
2007	185,000	14,656
2008	150,000	6,562
Total	\$ 515,000	\$ 43,750

	Issuance Date	Interest Rates	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Loans payable							
<i>Governmental Activities:</i>							
Emergency loans payable	7/1/1985	variable	\$ 34,000	\$ -	\$ 34,000	\$ -	\$ -
ULA loan payable	8/1/1989	none	67,286	-	67,286	-	-
Core Communities loan payable	7/27/2001	6.00%	200,000	-	-	200,000	-
HUD Section 108 loan (Modern Plastics)	10/31/2002	variable	450,000	-	100,000	350,000	200,000
HUD Section 108 loan (Family Dollar)	12/14/2004	variable	-	50,000	-	50,000	-
HUD Section 108 loan (Spence Technology)	2/28/2005	variable	-	100,000	-	100,000	-
USDA note payable	8/6/2004	4.75%	-	80,000	-	80,000	14,000
			<u>\$ 751,286</u>	<u>\$ 230,000</u>	<u>\$ 201,286</u>	<u>\$ 780,000</u>	<u>\$ 214,000</u>

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Annual debt service requirements to maturity for loans payable are as follows:

Years Ending December 31	Governmental Activities	
	Principal	Interest
2006	\$ 214,000	\$ 21,927
2007	115,000	14,011
2008	116,000	9,674
2009	119,079	8,288
2010	26,631	12,538
2011 - 2015	51,782	49,793
2016 - 2020	69,742	31,831
2021 - 2024	67,766	8,415
Total	\$ 780,000	\$ 156,476

	Issuance Date	Interest Rates	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Capital leases							
<i>Governmental Activities:</i>							
Dump trucks	2/8/2001	6.96%	\$ 91,029	\$ -	\$ 22,020	\$ 69,009	\$ 23,593
Photocopiers	4/10/2004	4.60%	118,866	-	29,724	89,142	31,121
Computers	11/22/2004	8.87%	-	80,481	14,512	65,969	27,839
Telephone system	10/28/2004	5.44%	-	199,200	24,333	174,867	36,780
			<u>\$ 209,895</u>	<u>\$ 279,681</u>	<u>\$ 90,589</u>	<u>\$ 398,987</u>	<u>\$ 119,333</u>
<i>Business-type Activities:</i>							
Cemetery equipment	3/6/2001	6.00%	\$ 30,872	\$ -	\$ 10,306	\$ 20,566	\$ 11,730
Photocopier	6/10/2004	9.35%	3,188	-	768	2,420	825
			<u>\$ 34,060</u>	<u>\$ -</u>	<u>\$ 11,074</u>	<u>\$ 22,986</u>	<u>\$ 12,555</u>

Annual debt service requirements to maturity for capital leases are as follows:

Years Ending December 31	Governmental Activities		Business-Type Activities	
	Principal	Interest	Principal	Interest
2006	\$ 119,333	\$ 18,846	\$ 12,555	\$ 1,016
2007	124,868	13,312	9,723	266
2008	96,535	5,771	708	21
2009	43,291	2,102	-	-
2010	14,960	171	-	-
Total	\$ 398,987	\$ 40,201	\$ 22,986	\$ 1,303

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Long-term debt activity can be summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities					
Loans payable	\$ 751,286	\$ 230,000	\$ 201,286	\$ 780,000	\$ 214,000
Capital leases	209,895	279,681	90,589	398,987	119,333
Compensated absences	295,954	288,189	252,067	332,076	283,000
Total Governmental Activities	<u>\$ 1,257,135</u>	<u>\$ 797,870</u>	<u>\$ 543,942</u>	<u>\$ 1,511,063</u>	<u>\$ 616,333</u>
Business-type Activities					
General obligation bonds	\$ 685,000	\$ -	\$ 170,000	\$ 515,000	\$ 180,000
Capital leases	34,060	-	11,074	22,986	12,555
Deferred amount on refunding	(26,288)	-	(6,858)	(19,430)	(6,858)
Compensated absences	54,659	60,784	51,805	63,638	60,000
Total Business-type Activities	<u>\$ 747,431</u>	<u>\$ 60,784</u>	<u>\$ 226,021</u>	<u>\$ 582,194</u>	<u>\$ 245,697</u>

For governmental activities, compensated absences are typically liquidated by the General Fund.

9. RISK MANAGEMENT

The City is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The City has purchased commercial insurance for all of these various risks. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

10. PENSION PLAN – GENERAL EMPLOYEES' RETIREMENT SYSTEM

Plan Description

The General Employees' Pension Plan is a single-employer defined benefit pension plan that is administered by the City of Benton Harbor General Employees' Retirement System. This Plan covers all appointed officers and employees of the City (except personnel of the Fire and Police departments) and appointed officers and employees of the Southwest Michigan Regional Airport Authority. The system provides retirement, disability and death benefits to Plan members and their beneficiaries. At July 1, 2004, the date of the most recent actuarial valuation, membership consisted of 42 retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them, and 83 current active employees. The plan does not issue a separate financial report.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Summary of Significant Accounting Policies

The financial statements of the Plan are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. The City's contributions are recognized when due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. All plan investments are reported at fair value.

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the City's collective bargaining units and requires a contribution from the employees of 3 percent. The funding policy provides for periodic employer contributions at actuarially determined rates. Administrative costs of the Plan are financed through investment earnings.

Annual Pension Costs

For the year ended June 30, 2005, the City's annual pension cost of \$125,617 for the Plan was equal to the required and actual contribution. The annual required contribution was determined as part of an actuarial valuation at July 1, 2004, using the aggregate actuarial cost method. Significant actuarial assumptions used include: (a) a 7.75 percent investment rate of return; (b) projected salary increases of 4 percent per year; and (c) no cost of living adjustments. Both (a) and (b) include an inflation component. The actuarial value of assets was determined using fair market values. The unfunded actuarial liability is being amortized as a level percentage of payroll on a closed basis, over 30 years.

Three-year trend information as of June 30 follows:

	Fiscal Year Ended June 30		
	<u>2003</u>	<u>2004</u>	<u>2005</u>
Annual pension costs (APC)	\$ 97,228	\$ 93,006	\$ 125,617
Percentage of APC contributed	100%	100%	100%
Net pension obligation	\$ -	\$ -	\$ -

11. PENSION PLAN - POLICE AND FIRE RETIREMENT SYSTEM PLAN DESCRIPTION

Plan Description

The Police and Fire Pension Plan is a single-employer defined benefit pension plan that is administered by the City of Benton Harbor Police and Fire Employees Retirement system/this Plan covers all full-time police and fire employees of the City. The system provides retirement, disability and death benefits to Plan members and their beneficiaries. At July 1, 2004, the date of the most recent actuarial valuation, membership consisted of 60 retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them, and 34 current active employees. The Plan does not issue a separate financial report.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

Summary of Significant Accounting Policies

The financial statements of the Plan are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. The City's contributions are recognized when due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. All plan investments are reported at fair value.

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the City's collective bargaining units, and requires a contribution from the employees of 5 percent for police employees and 6 percent for fire employees. The funding policy provides for periodic employer contributions at actuarially determined rates. Administrative costs of the Plan are financed through investment earnings.

Annual Pension Cost

For the year ended June 30, 2005, the City's annual pension cost of \$214,644 for the Plan was equal to the City's actual and required contribution. In addition, \$258,063 was funded by the tax levy described below and recorded as "property taxes" on the Statement of Changes in Plan Net Assets. The annual required contribution was determined as part of an actuarial valuation at July 1, 2003, using the aggregate actuarial cost method. Significant actuarial assumptions used include (a) a 7.75 percent investment rate of return, (b) projected salary increases of 4 percent per year, and (c) 4 percent per year cost of living adjustments. Both (a) and (b) include an inflation component. The unfunded actuarial liability is being amortized as a level percentage of payroll on a closed basis. The remaining amortization period is 27 to 30 years.

On August 14, 1984, the Circuit Court for Berrien County ordered the City of Benton Harbor to pay off the then calculated \$2,597,299 unfunded liability over the next 30 years. The City must levy a sufficient additional millage on an annual basis to pay the portion of this 30 year amortization plus normal operating costs that are not covered under the general operating budget. As indicated above, during the year \$258,063 was recorded as property tax revenue. Due to the age of this commitment, the actuary has not included this as a net pension obligation.

Three-year trend information as of June 30 follows:

	<u>Fiscal Year Ended June 30</u>		
	<u>2003</u>	<u>2004</u>	<u>2005</u>
Annual pension costs (APC)	\$ 370,738	\$ 318,048	\$ 214,644
Percentage of APC contributed	100%	100%	100%
Net pension obligation	\$ -	\$ -	\$ -

12. CONTINGENCIES

The City is arbitrating several illegal discharge cases. In all of these cases, retroactive pay or pay adjustments may be required. Currently, the City is unable to presently predict the outcome of the range of potential loss, if any, which may result from the disposition of these matters.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Financial Statements

The City is also the defendant in various litigations involving wrongful death, challenges to various City ordinances, various real estate disputes, breach of contract and violation of civil rights. The civil suits will likely be covered by the City's liability insurance.

City management considers the City's exposure under all of the suits to be immaterial. No provision for any loss has been made in the financial statements.

13. CONSTRUCTION CODE FEES

The City oversees building construction, in accordance with the State's construction code act, including inspection of building codes. The City charges fees for these services. Beginning in January 1, 2000, the law requires that collection of these fees be used only for construction code costs, including an allocation of estimated overhead costs. A summary of the current year activity and the cumulative shortfall generated since January 1, 2000, is as follows:

Deficit - July 1, 2004	\$ (303,932)
Building permit revenue	61,168
Construction code expenses	<u>(142,298)</u>
Accumulated shortfall - June 30, 2005	<u><u>\$ (385,062)</u></u>

* * * * *

REQUIRED SUPPLEMENTARY INFORMATION

City of Benton Harbor, Michigan
Required Supplementary Information

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (A)	Actuarial Accrued Liability (B)	Unfunded AAL (UAAL) (A-B)	Funded Ratio (A/B)	Covered Payroll (C)	UAAL as a % of Covered Payroll
<u>General Employees' Retirement System</u>						
6/30/1998	\$ 5,812,916	\$ 3,677,567	\$ 2,135,349	158.1%	\$ 2,235,027	-n/a-
6/30/2000	6,674,675	5,245,864	1,428,811	127.2%	2,506,666	-n/a-
6/30/2001	6,167,942	5,541,517	626,425	111.3%	2,533,613	-n/a-
6/30/2002	6,253,841	6,173,546	80,295	101.3%	2,610,223	-n/a-
6/30/2003	6,436,460	6,276,034	160,426	102.6%	2,592,799	-n/a-
6/30/2004	6,548,522	6,569,423	(20,901)	99.7%	2,805,811	0.7%

Police and Fire Retirement System

6/30/1998	10,089,128	9,030,330	1,058,798	111.7%	1,515,908	-n/a-
6/30/2000	10,856,074	10,811,520	44,554	100.4%	1,346,128	-n/a-
6/30/2001	10,004,228	11,672,480	(1,668,252)	85.7%	1,351,244	123.5%
6/30/2002	10,210,869	12,109,175	(1,898,306)	84.3%	1,231,468	154.1%
6/30/2003	10,235,411	11,884,761	(1,649,350)	86.1%	1,349,989	122.2%
6/30/2003	10,184,702	14,548,269	(4,363,567)	70.0%	1,439,856	303.1%

Schedule of Employer Contributions

<u>Year Ended June 30</u>	<u>Annual Required Contributions</u>	<u>Percentage Contributed</u>
<u>General Employees' Retirement System</u>		
2000	\$ -	100%
2001	-	100%
2002	-	100%
2003	97,228	100%
2004	93,006	100%
2005	125,617	100%
<u>Police and Fire Retirement System</u>		
2000	\$ 18,361	100%
2001	45,584	100%
2002	362,562	100%
2003	370,738	100%
2004	318,048	100%
2005	214,644	100%

COMBINING AND INDIVIDUAL FUND FINANCIAL
STATEMENTS and SCHEDULES

City of Benton Harbor, Michigan
Combining Balance Sheet
Nonmajor Governmental Funds
June 30, 2005

	Special Revenue		
	Major Streets	Local Streets	Federal Grants
Assets			
Cash and cash equivalents	\$ 827	\$ -	\$ 17,796
Accounts receivable	-	-	1,321
Due from other governments	114,602	31,833	251,109
Due from other funds	288,697	-	-
Advances to other funds	328,693	-	-
<u>TOTAL ASSETS</u>	<u>\$ 732,819</u>	<u>\$ 31,833</u>	<u>\$ 270,226</u>
<u>LIABILITIES AND FUND BALANCES</u>			
Liabilities			
Accounts payable	\$ 4,955	\$ 9,195	\$ 87,161
Accrued liabilities	5,915	8,056	14,725
Due to other funds	165,563	-	328,596
Advances from other funds	285,534	328,693	49,825
Deferred revenue	-	-	167,418
Total liabilities	461,967	345,944	647,725
Fund balances (deficit)			
Reserved for advances	328,693	-	-
Unreserved, undesignated (deficit)	(57,841)	(314,111)	(377,499)
Total fund balances (deficit)	270,852	(314,111)	(377,499)
<u>TOTAL LIABILITIES, AND FUND BALANCES</u>	<u>\$ 732,819</u>	<u>\$ 31,833</u>	<u>\$ 270,226</u>

<u>State Grants</u>	<u>Debt Service</u>	<u>Permanent Public Improvement</u>	<u>Totals</u>
\$ -	\$ 3,311	\$ 180	\$ 22,114
-	-	-	1,321
-	-	-	397,544
2,879	954,411	228,451	1,474,438
-	-	324,655	653,348

\$ 2,879	\$ 957,722	\$ 553,286	\$ 2,548,765
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\$ -	\$ -	\$ 1,310	\$ 102,621
-	-	-	28,696
-	-	-	494,159
68,900	-	-	732,952
-	-	-	167,418

68,900	-	1,310	1,525,846
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-	-	324,655	653,348
(66,021)	957,722	227,321	369,571

(66,021)	957,722	551,976	1,022,919
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\$ 2,879	\$ 957,722	\$ 553,286	\$ 2,548,765
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City of Benton Harbor, Michigan
Combining Statement of Revenue, Expenditures and Changes in Fund Balances
Nonmajor Governmental Funds
For the Year Ended June 30, 2005

	Special Revenue		
	Major Streets	Local Streets	Federal Grants
Revenue			
Taxes and special assessments	\$ -	\$ -	\$ -
Federal sources	-	-	842,940
State sources	639,519	196,775	-
Interest	599	-	-
Total revenue	640,118	196,775	842,940
Expenditures			
Current:			
Public works:			
Road maintenance	378,094	408,719	-
Administration	19,873	18,484	-
Community and economic development	-	-	1,006,401
Debt service:			
Principal	-	-	-
Interest	-	-	3,976
Total expenditures	397,967	427,203	1,010,377
Revenue over (under) expenditures	242,151	(230,428)	(167,437)
Other financing sources (uses)			
Transfers in	-	119,720	-
Transfers (out)	(119,720)	-	-
Total other financing sources	(119,720)	119,720	-
Net changes in fund balances	122,431	(110,708)	(167,437)
Fund balances (deficit), beginning of year	148,421	(203,403)	(210,062)
Fund balances (deficit), end of year	\$ 270,852	\$ (314,111)	\$ (377,499)

<u>State Grants</u>	<u>Debt Service</u>	<u>Permanent Public Improvement</u>	<u>Totals</u>
\$ -	\$ 420,000	\$ 161,551	\$ 581,551
-	-	-	842,940
-	-	-	836,294
-	128	8	735
-	420,128	161,559	2,261,520
-	-	-	786,813
-	-	-	38,357
-	-	37,375	1,043,776
-	101,286	-	101,286
-	2,654	-	6,630
-	103,940	37,375	1,976,862
-	316,188	124,184	284,658
-	-	-	119,720
-	-	-	(119,720)
-	-	-	-
-	316,188	124,184	284,658
(66,021)	641,534	427,792	738,261
\$ (66,021)	\$ 957,722	\$ 551,976	\$ 1,022,919

City of Benton Harbor, Michigan
Combining Statement of Fiduciary Net Assets
Pension Trust Funds
June 30, 2005

	General Employees' Retirement System	Police and Fire Retirement System	Totals
Assets			
Cash and cash equivalents	\$ 45,070	\$ 26,222	\$ 71,292
Investments:			
Fixed income securities	2,121,875	3,429,949	5,551,824
Equities	3,669,483	5,943,737	9,613,220
Money market	206,265	319,590	525,855
Receivables:			
Accrued interest	13,524	21,874	35,398
Other	365,797	191,418	557,215
 Total assets	 6,422,014	 9,932,790	 16,354,804
 Liabilities			
Due to resigned employees	41,708	19,179	60,887
 Net Assets			
Held in trust for pension benefits and other purposes	\$ 6,380,306	\$ 9,913,611	\$ 16,293,917

City of Benton Harbor, Michigan
Combining Statement of Changes in Fiduciary Net Assets
Pension Trust Funds
For the Year Ended June 30, 2005

	General Employees' Retirement System	Police and Fire Retirement System	Totals
Additions			
Taxes	\$ -	\$ 258,063	\$ 258,063
Contributions:			
Employer	125,617	214,644	340,261
Employee	89,277	105,195	194,472
Total contributions	214,894	319,839	534,733
Investment earnings:			
Net appreciation in fair value of investments	208,712	340,969	549,681
Interest and dividends	231,833	372,542	604,375
Net investment earnings	440,545	713,511	1,154,056
Total additions	655,439	1,291,413	1,946,852
Deductions			
Pension benefits paid directly to participants	305,025	863,830	1,168,855
Administrative expenses	95,670	109,568	205,238
Total deductions	400,695	973,398	1,374,093
Change in net assets	254,744	318,015	572,759
Net assets, beginning of year	6,125,562	9,595,596	15,721,158
Net assets, end of year	\$ 6,380,306	\$ 9,913,611	\$ 16,293,917

City of Benton Harbor, Michigan



Berrien County

SINGLE AUDIT

For the Year Ended June 30, 2005



REHMANN ROBSON

Certified Public Accountants

CITY OF BENTON HARBOR, MICHIGAN SINGLE AUDIT

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REHMANN ROBSON

Certified Public Accountants

A member of **THE REHMANN GROUP**



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

February 10, 2006

Honorable Mayor and Members
of the City Commission
City of Benton Harbor, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the *City of Benton Harbor, Michigan* as of and for the year ended June 30, 2005, which collectively comprise the City's basic financial statements, and have issued our report thereon dated February 10, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Benton Harbor, Michigan's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the City's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the accompanying schedule of findings and questioned costs as Item 2005-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matter in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness.

However, we noted other matters involving the internal control over financial reporting that we have reported to the management of the City of Benton Harbor, Michigan in a separate letter dated February 10, 2006.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Benton Harbor, Michigan's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, management, others within the organization, the City Commission, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style.



REHMANN ROBSON

Certified Public Accountants

A member of **THE REHMANN GROUP**



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH
REQUIREMENTS APPLICABLE TO MAJOR PROGRAMS
AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH OMB CIRCULAR A-133**

February 10, 2006

Honorable Mayor and Members
of the City Commission
City of Benton Harbor, Michigan

Compliance

We have audited the compliance of the *City of Benton Harbor, Michigan* with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal programs for the year ended June 30, 2005. The City of Benton Harbor, Michigan's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal programs is the responsibility of the City of Benton Harbor, Michigan's management. Our responsibility is to express an opinion on the City of Benton Harbor, Michigan's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Benton Harbor, Michigan's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Benton Harbor, Michigan's compliance with those requirements.

In our opinion, the City of Benton Harbor, Michigan, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2005.

Internal Control Over Compliance

The management of Benton Harbor, Michigan is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Benton Harbor, Michigan's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted a matter involving the internal control over compliance and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the City's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. The reportable condition is described in the accompanying schedule of findings and questioned costs as item 2005-2.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. We do not consider the matter referred to above to be a material weakness.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the *City of Benton Harbor, Michigan* as of and for the year ended June 30, 2005, and have issued our report thereon dated February 10, 2006. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements, taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the audit committee, management, others within the organization, the City Commission, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



CITY OF BENTON HARBOR, MICHIGAN

Schedule of Expenditures of Federal Awards

For the Year Ended June 30, 2005

Federal/Pass-through Grantor Program Title	CFDA Number	Federal/ Pass-through Grantor Number	Federal Expenditures
U.S. Department of Agriculture			
Direct Program:			
Rural Housing Service Community Facilities Loans and Grants	10.766	- n/a -	\$ 80,000
Rural Housing Service Community Facilities Loans and Grants	10.766	- n/a -	<u>65,000</u>
Total U.S. Department of Agriculture			145,000
U.S. Department of Housing and Urban Development			
Direct Programs:			
Community Development Block Grant			
Program year 2002-2003	14.218	B-02-MC-26-0035	53,453
Program year 2003-2004	14.218	B-03-MC-26-0035	584,000
Program year 2004-2005	14.218	B-04-MC-26-0035	242,750
Section 108 Loan Guarantee Program	14.218	B-98-MC-26-0035	150,000
Brownfield Economic Development	14.248	B-96-MC-26-0035	<u>130,155</u>
Total U.S. Department of Housing and Urban Development			1,160,358
U.S. Department of Justice			
Direct Program:			
COPS in School	16.710	2004-SH-WX-0153	<u>115,330</u>
Total Expenditures of Federal Awards			<u><u>\$ 1,420,688</u></u>

See Notes to Schedule of Expenditures of Federal Awards.

CITY OF BENTON HARBOR, MICHIGAN

Notes to Schedule of Expenditures of Federal Awards

1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal awards programs of the City of Benton Harbor, Michigan (the "City"). Federal awards received directly from federal agencies, as well as federal awards passed through other government agencies, are included on the schedule.

The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

The City of Benton Harbor reporting entity is defined in Note 1 of the City's financial statements.

2. SUBRECIPIENTS

The City of Benton Harbor did not provide federal awards to external subrecipients during the current year.

* * * * *

CITY OF BENTON HARBOR, MICHIGAN

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2005

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified? _____ yes X no

Reportable condition(s) identified
not considered to be material weaknesses? X yes _____ none reported

Noncompliance material to financial statements
noted? _____ yes X no

Federal Awards

Internal Control over major programs:

Material weakness(es) identified? _____ yes X no

Reportable condition(s) identified
not considered to be material weaknesses? X yes _____ none reported

Type of auditors' report issued on compliance
for major programs: Unqualified

Any audit findings disclosed that are required
to be reported in accordance with
Circular A-133, Section 510(a)? _____ yes X no

CITY OF BENTON HARBOR, MICHIGAN

Schedule of Findings and Questioned Costs (Continued)

For the Year Ended June 30, 2005

SECTION I - SUMMARY OF AUDITORS' RESULTS (Concluded)

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
14.218	Community Development Block Grant
Dollar threshold used to distinguish between Type A and Type B programs:	<u>\$300,000</u>
Auditee qualified as low-risk auditee?	_____ yes <u> X </u> no

SECTION II – FINANCIAL STATEMENT FINDINGS

2005-1 Internal Controls Over Cash Disbursements

In our testing of internal controls over cash disbursements, we found that the City is not consistently applying its own policies. Out of a sample of 212 disbursements tested, we noted that 80 items were missing check requests, posting instructions, and/or authorizing signatures. This condition creates the risk that disbursements may be made improperly and not be detected by management.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

2005-2 HUD – Community Development Block Grant – Allowable Costs

The condition described above applies to a major Federal program. In our testing of disbursements for the CDBG program, we noted that approximately 23% of the disbursements were missing one or more required elements of internal approval. While it appears that all disbursements were for eligible grant activities, this lack of consistent internal controls over cash disbursements creates the risk that Federal funds could be improperly disbursed, and not be detected by management.

No costs were questioned in the current year as a result of this finding.

CITY OF BENTON HARBOR, MICHIGAN

Schedule of Findings and Questioned Costs (Concluded)

For the Year Ended June 30, 2005

SECTION IV – PRIOR YEAR FINDINGS

Financial Statement Findings

None.

Federal Award Findings

2004-1 HUD - CDBG Davis-Bacon Compliance

In the report on the City's 2004 single audit, it was noted that the City was not retaining sufficient documentation to demonstrate it was complying with the prevailing wage requirements of the Davis-Bacon Act.

The City took corrective action to resolve this issue and began retaining the required information subsequent to June 30, 2004. For the 2005 audit, all required documentation to demonstrate compliance was readily available. Accordingly, this finding has been resolved to the auditors' satisfaction.

* * * * *



REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



February 10, 2006

To the Honorable Mayor of the
Member of the City Commission
Benton Harbor, Michigan

We have audited the financial statements of the **City of Benton Harbor** for the year ended June 30, 2005, and have issued our report thereon dated February 10, 2006. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America

As stated in our engagement letter dated August 16, 2005, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

In planning and performing our audit, we considered the City of Benton Harbor's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

As part of obtaining reasonable assurance about whether the City of Benton Harbor's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the City of Benton Harbor's compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each of its major federal programs for the purpose of expressing an opinion on City of Benton Harbor's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on City of Benton Harbor's compliance with those requirements.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City of Benton Harbor are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the City of Benton Harbor during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- Management's estimate of the useful lives of depreciable capital assets is based on the length of time it is believed that those assets will provide some economic benefit in the future. We evaluated the key factors and assumptions used to develop the useful lives of those assets in determining that they are reasonable in relation to the financial statements taken as a whole.
- Management's estimate of the various allowance made for uncollectible accounts receivable is based on past collection history. We evaluated the key factors and assumptions used to develop the allowances in determining that they are reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the City of Benton Harbor's financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by the City of Benton Harbor, either individually or in the aggregate, indicate matters that could have a significant effect on the City of Benton Harbor's financial reporting process.

In addition, the attached schedule summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to the governmental unit’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City of Benton Harbor’s auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This letter and the accompanying memorandum is intended for the use of the City Commission and management of the City of Benton Harbor, the State of Michigan, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

A handwritten signature in black ink, appearing to read "Lehmann Johnson", written in a cursive style.

City of Benton Harbor

Comments and Recommendations

For the Year Ended June 30, 2005

During our audit we became aware of certain issues regarding internal control and financial reporting. This memorandum summarizes our comments and suggestions regarding these matters. This memorandum does not affect our report dated February 10, 2006 on the financial statements of the City of Benton Harbor.

Overall Financial Condition

As management is keenly aware, the City has been experiencing some extremely tough economic times. Despite having placed a deficit elimination plan in effect (as disclosed in Note 2 to the financial statements), during the year ended June 30, 2005, the City's accumulated unreserved fund deficit in the general fund grew by almost one million dollars to more than \$3 million. In addition, the City reported fund deficits totaling \$942,367 in six other funds. On a full accrual perspective, the City's combined governmental activities reported an unrestricted deficit in net assets of \$2.4 million.

This condition contributed to the City's inability to make certain required payments to other units of government in a timely manner throughout the year, and continues to raise concerns about the City's financial solvency and its ongoing ability to provide and finance key governmental services.

Obviously, there is no easy solution for the City's current financial condition. Nevertheless, we recommend that the City continue to make rebuilding its fiscal solvency one of its most paramount objectives over the next few years.

Periodic Account Analyses

As noted in the prior year, the City has not been performing monthly account analyses or reconciliations for many of its balance sheet accounts. Our review of the general ledger revealed that a significant effort was again undertaken at year end to substantially adjust the City's accounting records to present information in accordance with generally accepted accounting principles.

While we were ultimately satisfied that the amounts presented in the City's audited financial statements were fairly presented in all material respects, the significant amount of corrections required at year end underscores that the interim financial data available to City management is not materially accurate or reliable.

One of the best internal control procedures for verifying the accuracy of the City's financial information through the year is the periodic analysis of account balances (particularly for balance sheet accounts) to ascertain the following:

- Balance sheet accounts are supported by itemized listings of the components comprising the financial statement totals;
- The detail listing is free of obvious errors, unusual reconciling items that suggest the need for adjustment, and mispostings or other clerical errors;
- The balances make sense relative to operational data

City of Benton Harbor

Comments and Recommendations

For the Year Ended June 30, 2005

Accordingly, we repeat our recommendation that all balance sheet accounts be analyzed monthly. The analyses should be retained and reviewed by a responsible official other than the preparer as part of the monthly closing cycle. This procedure will provide improved assurance that accounting errors will be detected and corrected in a timely manner, and will provide management and the City Commission more meaningful and useful financial data with which to make their decisions.

Internal Controls – Segregation of Duties

Management is responsible for establishing and maintaining effective internal control over financial reporting and the safeguarding of the City's assets. In establishing appropriate internal controls, careful consideration must be given to the cost of a particular control and the related benefits to be received. Accordingly, management must make the difficult decision of what degree of risk it is willing to accept, given the government's unique circumstances.

As is the case with many organizations of similar size, the City lacks a sufficient number of accounting personnel in order to ensure a complete segregation of duties within its accounting function. Ideally, no single individual should ever be able to authorize a transaction, record the transaction in the accounting records, and maintain custody of the assets resulting from the transaction. Effectively, proper segregation of duties is intended to prevent an individual from committing an act of fraud or abuse and being able to conceal it.

Events of recent years have given rise to a heightened awareness of the risks of fraud and abuse, especially in the governmental environment, where public accountability is at its highest. The purpose of internal controls is to provide reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are properly authorized and recorded. Any limitations on the effectiveness of a government's internal controls carries with it a greater risk of fraud and abuse.

As stated previously, the establishing and maintaining of internal controls is the responsibility of management. As the City's independent external auditors, we are specifically banned by professional standards from performing any management functions. In other words, the annual audit is not a part of the City's internal control structure, and cannot not be relied upon as part of *management's* systems to deter or detect fraud and abuse.

While there are, of course, no easy answers to the challenge of balancing the costs and benefits of internal controls and the segregation of duties, we would nevertheless encourage management to actively seek ways to further strengthen its internal control structure by requiring as much independent review, reconciliation, and approval of accounting functions by qualified members of management as possible.

City of Benton Harbor

Comments and Recommendations

For the Year Ended June 30, 2005

Approval for Disbursements

In addition to the general internal control considerations described in the previous comment, during our testing of internal controls over cash disbursements, we found that the City is not consistently applying its own policies. Out of a sample of 212 disbursements tested, we noted that 80 items were missing check requests, posting instructions, and/or authorizing signatures. This condition creates the risk that disbursements may be made improperly and not be detected by management.

Refunding of Employee Contributions to the Pension System

Our review of the City's liability accounts revealed some rather old balances related to amounts owed to terminated employees. When an employee leaves the City, he or she is entitled to a refund of any employee contributions made to the retirement system. However, under the City's current operating procedure, these amounts are only disbursed upon specific request of the employee. If an employee fails to request this payment, the City does not make any effort to locate the employee or disburse the funds. Accordingly, the City is currently holding balances for individual employees that are up to 15 years old. We recommend that the City provide each employee with the necessary paperwork to request a distribution of employee contributions to the pension system at the time of separation from the City. If an employee does not file a request for these funds within a reasonable timeframe, such amounts should be escheated in accordance with state law.

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